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Acquisitions of Pennsylvania Bank Holding Companies-Who Determines What Is Best for the Community?

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I. Introduction

Have you ever been to a hockey game at the *First Union Center* in Philadelphia? Do you expect that you may someday take in a Sunday afternoon baseball game at *PNC Park* on the north side of Pittsburgh? While banks have sought to increase their commercial exposure by displaying their names on Pennsylvania sports arenas, for many of the Commonwealth's citizens, and Americans as a whole, banking plays a much larger role in daily life beyond that of sponsoring popular sporting events. Its historical importance has prompted the Supreme Court to note that banking is of a profound concern to local communities throughout the United States.[1] Despite this profound local importance however, Congress appears to believe that the communities' interests are best advanced when policy decisions are made at the federal level.

In the 1990s, Congress has taken measures to promote interstate bank holding company acquisitions. Changes in federal law, such as the passage of the Riegle-Neal Interstate Banking and Branching Act of 1994[2] (IBBEA), have sought to increase the likelihood that bank holding company acquisitions will occur. Congress hoped to achieve its goal through the repeal of federal legislation that provided the states with the authority to govern the terms under which bank holding company acquisitions would occur.[3] The rapid response to Congressional policy is evident by

1. *See* Northeast Bancorp., Inc. v. Board of Governors of the Federal Reserve Sys., 472 U.S. 159, 177 (1985) (citing Lewis v. B.T. Inv. Managers, Inc., 447 U.S. 27, 38 (1980)).

2. Pub. L. No. 103-328, § 101, 108 Stat. 2339, 2339-2381 (1994).

3. *See* Patrick Mulloy & Cynthia Lasker, *The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994: Responding to Global Competition,* 21 LEGIS. 255, 269 (1995).

the increase of acquisition activity in the banking field in recent years.[4]

The banking environment in Pennsylvania has not been sheltered from the spur of acquisition activity. One of Pennsylvania's largest banking concerns, Philadelphia-based Corestates Financial, was acquired by North Carolina's First Union in April of 1998.[5] Following First Union's acquisition of Corestates, Pennsylvania, once home to three large banking concerns, now harbors only two.[6] The acquisition of Corestates, along with a recent bid from the Bank of New York for Mellon[7] provides evidence of the uncertain future of Pennsylvania bank holding companies. Even though Bank of New York was ultimately unsuccessful in its attempt to acquire Mellon in the spring of 1998, many analysts consider Mellon to remain a probable target of further acquisition plans.[8]

While federal legislation promotes the banking atmosphere of the 1990's, some in Pennsylvania's legislature appear to disapprove of the current trend. In the 182nd Assembly, the Pennsylvania Senate passed legislation that would require State Banking Department approval for any acquisition of a Pennsylvania bank holding company with assets of ten billion dollars.[9] Despite its questionable validity in light of Congressional amendments to the Federal Bank Holding Company Act[10] however, the amended version of the bill died in the House.[11]

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4. *See* Lee Meyerson & Maripat Alpuche, *Structural Defenses to Unsolicited Takeover Offers and Bids in the Banking Industry*, 922 P.L.I./CORP. 77, 79 (1996).

5. *See Acquisition is Completed of Corestates Financial*, WALL ST. J., Apr. 29, 1998, at B4.

6. *See* 36 PA. LEGIS. J.-S. 2050, 2052-54, 182nd Legis. Sess. (June 8, 1998) (senate debate discussing the need for legislation to protect Pennsylvania's largest bank holding companies from hostile takeovers). The two largest Pennsylvania bank holding companies are Mellon Bank Corp. and PNC Bank Corp. *See id.*

7. *See* Patricia Sabatini, *Spurned Suitor Ends Bid for Mellon: Bank of New York Never Got to Bargain $23 Billion Offer*, PITTSBURGH POST GAZ., May 21, 1998, at A1.

8. *See* Matt Murray & Stephen E. Frank, *Bank of New York Withdraws Its Bid for Mellon*, THE WALL ST. J., May 21 1998, at A3; *see also* Arnold G. Danielson, *National Trends In Banking: The Battle for Supremacy*, 17 No. 2 BANKING POL'Y REP. 1, 12 (1998) (listing Mellon as a logical bank target).

9. *See* 36 PA. LEGIS. J.-S. 2050, 2056, 182nd Legis. Sess. (June 8, 1998). The amended version of the bill passed the Senate by a vote of 43 for and 5 opposed. *See id.*

10. 12 U.S.C. §§ 1841-1850 (1994).

11. *See* H.R. 1479, 182nd Legis. (Pa. 1998). The bill died at the close of the 182nd Assembly.

The proponents of the failed legislation need not fret however, Pennsylvania's business corporation laws may already provide that the Commonwealth's interests will not go unheard when a predator from outside the Commonwealth's borders appears positioned to pounce upon a Pennsylvania bank holding company.[12] One of the provisions passed pursuant to Pennsylvania's stringent fourth-generation antitakeover legislation involved refining Pennsylvania's definition of fiduciary duty.[13] Pennsylvania's fiduciary duty law expressly allows boards of directors to exercise their duties and make decisions based on the interests of the communities in which the corporations conduct operations.[14]

Congress however, does not appear to share Pennsylvania's trust in directors of corporations to consider the needs of the community, at least not in the banking area. Under the Bank Holding Company Act, Congress has given regulatory authority over acquisitions of bank holding companies to the Board of Governors of the Federal Reserve Board.[15] Under the federal legislative scheme, the Board of Governors of the Federal Reserve Board, not the boards of directors of bank holding companies, is entrusted with the task of protecting community interests and the public welfare in the event of a bank holding company acquisition.[16]

When a Pennsylvania bank holding company finds itself a target of a hostile takeover attempt, may Pennsylvania allow the board of directors to assess the needs of the community and take actions on its behalf, the task to which Congress has delegated responsibility for the Federal Reserve Board? In an effort to answer this question, Part II reviews federal legislation providing

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12. *See* 15 PA. CONS. STAT. ANN. § 1715(a) (West 1995). Pennsylvania's antitakeover legislation provides significant protection from hostile takeover attempts to the Commonwealth's bank holding companies. *See* Murry & Frank, *supra* note 8, at A3 (noting the difficulty Bank of New York would face in attempting a hostile takeover of Mellon); *see also* Gary M. Holihan, Note, *Pennsylvania's Antitakeover Statute: An Impermissible Regulation of the Interstate Market for Corporate Control,* 66 CHI.-KENT L. REV. 863, 863 (1992) (calling Pennsylvania's antitakeover legislation the "nation's toughest antitakeover statute").

13. *See* Gary M. Holihan, *supra* note 12, at 883. Under Pennsylvania's most recent antitakeover legislation, when faced with a potential takeover situation boards of directors may consider factors other than shareholder profit. *See id; see also* title 15, § 1715.

14. *See* title 15, § 1715(a)(1).

15. *See* 12 U.S.C. § 1842(a) (1994).

16. *See id.* § 1842(c)(2); *see also* S. REP. NO. 1095, at 10 (1955), *reprinted in* 1956 U.S.S.C.A.N. 2482, 2491-92 (discussing how Federal Reserve Board regulation would ensure that the expansion of bank holding companies "would be regulated in the public interest").

for regulation of bank holding companies, Part III discusses Pennsylvania's fiduciary law, and Part IV considers the question of federal preemption.

II. Bank Holding Company Regulation: Protecting Community Interests

Nationally chartered banks are created and governed primarily by the National Bank Act.[17] Bank holding companies however, are governed by the Bank Holding Company Act (BHCA).[18] "Bank holding company" is defined in the BHCA as "any company which has control over any bank."[19] A bank holding company may be organized as a corporation, partnership, business trust, association, or any other similar organization.[20] Two of Pennsylvania's largest bank holding companies are organized as Pennsylvania corporations.[21]

A company has control over a bank when the company: (1) directly or indirectly controls, or has the power to vote more than 25% of any class of securities of a bank;[22] (2) the company controls the election of a majority of the directors or trustees of a bank;[23] or (3) the Board of Governors of the Federal Reserve Board determines that a company exercises a controlling influence over a bank.[24]

While mergers, consolidations, and other acquisitions of national banks are subject to the approval of the Comptroller of the Currency,[25] under the Bank Holding Company Act like

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17. *See id.* §§ 21-216.

18. *See id.* §§ 1841-1850.

19. *Id.* § 1841(a)(1). The definition of "bank" includes

> (A) An insured bank as defined in section 3(h) of the Federal Deposit Insurance Act [12 U.S.C. 1813(h)]
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> (B) An institution organized under the laws of the United States . . . which both
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> (i) accepts demand deposits or deposits that the depositor may withdraw by check or similar means for payment to third parties or others; and
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> (ii) is engaged in the business of making commercial loans.

12 U.S.C. § 1841(c)(1) (1994 & supp. II 1996). The Act also includes exceptions from the definition of "bank" excluding certain designated organizations. *See id.* § 1841(c)(2).

20. *See id.* § 1841(b).

21. *See* S.E.C. filing 10-Q, Mellon Bank Corp. (May 5, 1997); *see also* S.E.C. filing 10-K/A PNC Bank Corp. (June 24, 1998).

22. *See* 12 U.S.C. § 1841(a)(2)(A) (1994).

23. *See id.* § 1841(a)(2)(B).

24. *See id.* § 1841(a)(2)(C).

25. *See id.* §§ 215a, 215b, 215c (1994 & Supp. II 1996).

transactions involving bank holding companies must receive authorization from the Governors of the Federal Reserve Board.[26] According to the legislative history of the Bank Holding Company Act, because of the importance of banking to the nation, Congress requires Federal Reserve Board regulation of bank holding companies in order to protect the public welfare.[27] Section 1842 of the Bank Holding Company Act provides that

> It shall be unlawful, except with the prior approval of the Board(1) for any action to be taken that causes any company to become a bank holding company; (2) for any action to be taken that causes a bank to become a subsidiary of a bank holding company; (3) for any bank holding company to acquire direct or indirect ownership or control of any voting shares of any bank if, after such acquisition, such a company will directly or indirectly own or control more than 5 per centum of the voting shares of such bank; (4) for any bank holding company or subsidiary thereof, other than a bank, to acquire all or substantially all of the assets of a bank; or (5) for any bank holding company to merge or consolidate with any other bank holding company.[28]

Basically, any action that would have the effect of creation, merger, consolidation, or acquisition of a bank holding company must first receive the approval of the Board of Governors of the Federal Reserve Board.[29] Of particular relevance in a hostile takeover situation is part three, which requires Board approval for any transaction that would allow an acquiror to gain, whether directly or indirectly, more than 5% of the voting shares of a bank.[30]

The BCHA emphasizes the Board of Governor's role in protecting the public welfare when evaluating an application for a transaction of the type enumerated in section 1842.[31] In passing the BCHA, Congress established several factors, concentrating primarily on the proposed action's potential impact on the relevant community, that the Board of Governors must consider when

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26. *See id.* § 1842.

27. *See* S. REP. NO. 1095, at 10 (1955), *reprinted in* 1956 U.S.C.C.A.N. 2482, 2491.

28. 12 U.S.C. § 1842(a) (1994).

29. *See id.*

30. *See id.* § 1842(a)(3).

31. *See id.* §§ 1842(c)(1)(B), 1842(c)(2), & 1842(d)(3); *see also* S. REP. NO. 1095, at 10 (1955), *reprinted in* 1956 U.S.C.C.A.N. 2482, 2491.

judging an application.[32] For example, the Board is not to approve any proposal that may have the effect of substantially lessening competition in any section of the country unless the benefits to the convenience and needs of the community clearly outweigh any anticompetitive effects of the proposal.[33] Furthermore, the Board must take into consideration the applicant's record of compliance with the Community Reinvestment Act.[34] Under this requirement, the Board must consider the applicant's record of meeting the credit needs of the community, including those of low and moderate income neighborhoods.[35]

The BHCA also provides that the Board of Governors must take into consideration community factors throughout its decision making process.[36] In every case, the Board must consider "the convenience and needs of the community to be served."[37] Thus, the Board may not approve an application without considering the interests of the community involved.

The legislative history of the BCHA indicates that Congress was concerned about the development of bank holding companies and the impact their expansion may have on the nation.[38] In passing the BCHA, Congress sought to alleviate its fear by delegating to the Federal Reserve Board the responsibility of

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32. *See* 12 U.S.C. § 1842(c)(2) (1994). The Board must also consider the applicant's ability to provide information the Board may find appropriate in its consideration of the application. *See id.* § 1842(c)(3). If the applicant does not provide the Board with adequate assurances that the applicant will provide information that the Board may find appropriate in order to enforce compliance with the other factors, the Board shall not approve the application. *See id.* § 1842(c)(3)(A). The Board must also consider the management capabilities of the applicant. *See id.* § 1842(c)(2). For further elaboration of the evaluation criteria used by the Board of Governors when considering an application, *see* Federal Reserve Board Regulation Y.

33. *See* 12 U.S.C. § 1842(c)(1)(B) (1994). The Board is also not to approve any proposal that would have the effect of creating a monopoly or further any attempt at creating a monopoly in any part of the United States. *See id.* § 1842(c)(1)(A).

34. *See id.* § 1842(d)(3).

35. *See id.* § 1842(d)(3)(A) (stating that the Board must comply with its responsibilities under section 2903). Section 2903 of the Community Reinvestment Act states in part that

> In connection with its examination of a financial institution, the appropriate Federal financial supervisor agency shall
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> (1) assess the institution's record of meeting the credit needs of its entire community, including low- and moderate income neighborhoods consistent with the safe and sound operation of such institution;

Id. § 2903(a) (1994).

36. *See* 12 U.S.C. § 1842(c)(2) (1994).

37. *Id.*

38. *See* S. REP. NO. 1095, at 2 (1955), *reprinted in* 1956 U.S.C.C.A.N. 2482, 2483.

protecting the public interest.[39] Initially however, the states were left with a share of the responsibility.

A. The Douglass Amendment

Prior to 1994, the Bank Holding Company Act required the Board of Governors of the Federal Reserve Board to defer to state law when considering an application for a transaction of the type listed in section 1842.[40] Following the passage of the Douglas Amendment, the Board's decision upon evaluating an application depended, at least in part, on the laws of the home state of the target of the applicant.[41] The Amendment prohibited interstate acquisition of any voting shares, interests, or all or substantially all of the assets of a bank by a bank holding company unless such action was explicitly authorized by the state where the bank was located.[42] Thus, unless the proposed transaction was authorized by laws of the home state of the target bank, the Board could not approve an application.[43] As a result of the Amendment, interstate banking acquisitions were often barred by state legislation.[44]

Eventually some state legislatures began to permit interstate banking subject to certain regional and reciprocity requirements.[45] Under these arrangements, states would allow holding companies of only specifically designated states to acquire banks within their state, and for some, only so long as the home state of the foreign

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39. *See id.* at 9-11.

40. *See* 12 U.S.C. § 1842(d) (1988), *amended by*, The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994, 12 U.S.C. § 1842(d) (1994).

41. *See id.*

42. *See id.* The Douglas Amendment read in pertinent part that:

> Notwithstanding any other provision of this section, no application (except an application filed as a result of a transaction authorized under section 1823(f) of this title) shall be approved under this section which will permit any bank holding company or any subsidiary thereof to acquire, directly or indirectly, any voting shares of, interest in, or all or substantially all of the assets of any additional bank located outside of the State in which the operations of such bank holding company's banking subsidiaries were principally conducted on July, 1966, or the date on which such company became a bank holding company, whichever is later, unless the acquisition of such shares or assets of a State bank by an out-of-state bank holding company is specifically authorized by the statute laws of the State in which such bank is located, by language to that effect and not merely by implication.

Id.

43. *See id.*

44. *See* Mulloy & Lasker, *supra* note 3, at 258.

45. *See id.*

holding company allowed similar treatment to the bank holding companies of their state.[46] The Supreme Court validated these state regional and reciprocity laws in *Northeast Bancorp v. Board of Governors of the Federal Reserve System.*[47] The Court found that in light of the Douglass Amendment, such state legislative schemes were of the type contemplated by Congress.[48] Moreover, the Court determined that the laws in question were consistent with the broader purposes of the Bank Holding Company Act to "retain local, community-based control over banking."[49] Prior to 1995, similar legislation existed in Pennsylvania.[50] Nearly a decade after the Supreme Court's validation of the legislation however, Congress changed its attitude toward regional banking.

B. The Interstate Branching and Banking Efficiency Act of 1994

In the 1990's, some members of Congress began to express concerns with the banking system that had developed as a result of the varying state laws.[51] The fragmented system in the United States contrasted sharply with the banking systems of other major financial countries such as those in Canada, Japan, and the countries of Europe.[52] Former Treasury Secretary Lloyd Bentsen referred to the country's "patchwork system" of banking as "clumsy."[53] While many states had moved toward a greater acceptance of interstate bank holding company acquisitions, the variations in laws and regulations at the state level permitted interstate banking only in an inefficient and high cost manner.[54] In response to concerns about the efficiency of the banking system in the United States, Congress passed the Interstate Branching and Banking Efficiency Act of 1994.[55] With the passage of the Interstate Branching and Banking Efficiency Act (IBBEA),

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46. *See id.*

47. 472 U.S. 159 (1985).

48. *See id.* at 172.

49. *Id.* at 173.

50. *See* PA. STAT. ANN. tit. 7, §§ 115, 116 (West 1995), *amended by* PA. STAT. ANN. tit. 7, § 115 (West supp. 1998). The current statute contains no regional or reciprocity on bank acquisitions within the Commonwealth. *See* PA. STAT. ANN. tit. 7, § 115.

51. *See* S. REP. NO. 103-240, at 3, 4 (1994).

52. *See id.* at 4.

53. *Id.* at 10 (quoting Secretary Bensen).

54. *See id.* (quoting former Federal Reserve Board Governor John LaWare's testimony before the Senate Committee on Banking, Housing, and Urban Affairs on October 5, 1993).

55. *See generally id.*

Congress sought to reduce state control over interstate banking acquisitions.[56]

One of the more substantial changes introduced by the passage of the IBBEA was the repeal of the Douglass Amendment. Section 1842(d) of the Bank Holding Company Act now provides that, so long as an applicant bank holding company is adequately capitalized and managed, the Board of Governors of the Federal Reserve Board may approve an application "to acquire control of, or acquire all or substantially all of the assets of, a bank located in a State other than the home State or such bank holding company, without regard to whether such transaction is prohibited under the law of any State."[57] Thus, the IBBEA withdrew the state's permission under the Douglas Amendment to decide if and how interstate bank acquisitions would occur.[58]

The legislative history reveals that in passing the Interstate Branching and Banking Act, Congress sought to achieve benefits aimed toward creating additional consumer convenience and choices[59] and increase banks' ability to diversify risks through exposure to varying economic regions, thus lowering the possibility of bank failure and subsequent Federal government bailout.[60] In allowing the Federal Reserve Board of Governors to judge applications for interstate bank holding company acquisitions

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56. *See* S. REP. NO. 103-240, at 10 (1994).

57. 12 U.S.C. § 1842(d)(1)(A) (1994).

58. The IBBEA does however, enumerate certain areas where the Board of Governors must defer to state legislation. A host state may provide for a minimum amount of time that its banks be in existence before they may be acquired by an out-of-state bank holding company, *see id.* § 1842(d)(1)(B)(i), however the Federal Reserve Board may approve an acquisition of a bank that has been in existence for at least five years without regard to any state law requiring a longer period of time. *See id.* § 1842(d)(1)(B)(ii). Furthermore, state legislation requiring that a certain portion of bank assets be made available to state-sponsored housing entities is unaffected by the passage of the IBBEA, so long as the state requirements are not discriminatory, and were in effect prior to September 29, 1994. *See id.* § 1842(d)(1)(D). The Act specifically provides that it will have no effect on a state's ability to limit the percentage total amount of deposits of an insured depository institution held or controlled by any bank, bank holding company, or any of its affiliates, in the given state, to the extent such limitations are not discriminatory to out of-state banks, bank holding companies, or subsidiaries thereof. *See id.* § 1842(d)(2)(C). In addition, the Board must also be mindful of statewide concentration limits when applicant's are seeking an initial entry into a given state. *See* 12 U.S.C. § 1842(d)(2)(B) (1994). While Congress has expressly preserved some areas where state legislation may govern the outcome of the decision of the Board of Governors, the authority preserved by the IBBEA is nonetheless minimal compared to the control the states possessed under the Douglass Amendment.

59. *See* S. REP. NO. 103-240, at 12.

60. *See id.*

without regard to state law, the legislative history indicates that Congress felt the IBBEA would promote a banking environment that would better serve the community by fostering wider choices and better prices for consumers.[61]

In passing the IBBEA, Congress seems to have implied that varying state laws pertaining to the development of bank holding companies have not efficiently advanced the public interest. Despite Congressional action however, Pennsylvania appears unwilling to accept the proposition that the communities interest is sufficiently protected by the Federal Reserve Board.

III. Exercising Fiduciary Duty: Considering the Interests of the Community

As Congress has delegated the authority to consider the interests of the community, so too has the Pennsylvania legislature. While federal legislation gives the duty of protecting the interests of the public to the Board of Governors of the Federal Reserve Board,[62] Pennsylvania's legislature has given its corporations the authority to exercise their duties in the interest of the community.[63] Pennsylvania legislation permits boards of directors of Pennsylvania bank holding companies registered as Pennsylvania corporations to make decisions based on community interests.[64]

Section 1715 of the Pennsylvania Business Corporations Law states that boards of directors, committees of the board, and individual directors, in the discharge of their duties may consider "[t]he effects of any action upon the communities in which offices or other establishments of the corporation are located."[65] While

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61. *See id.* (quoting April 23, 1991 testimony of Federal Reserve Chairman Alan Greenspan).

62. *See* 12 U.S.C. §§ 1842(c)(2) & 1842(d)(3) (1994).

63. *See* 15 PA. CONS. STAT. ANN. § 1715(a)(1) (West 1995) (authorizing directors of corporations to consider interests of the community upon exercise of their duties).

64. *See id.*

65. *Id.* The entire section states that boards of directors, committees of the board, and individual directors, in the discharge of their duties, may consider

> (1) The effects of any action upon any or all groups affected by such action, including shareholders, employees, suppliers, customers and creditors of the corporation, and upon the communities in which offices or other establishments of the corporation are located.

Id. Pennsylvania law also allows directors to consider the short and long terms interests of the corporation, *see id.* § 1715(a)(2), the "resources, intent and conduct" of any person attempting to acquire control of the corporation, title 15, § 1715(a)(3), and "all other pertinent factors." *Id.* § 1715(a)(4). A shareholders group challenged the constitutionality

boards of directors, committees, and individual directors may of course consider the interests of the shareholders, they need not consider "the interests of any particular group affected . . . as a dominant or controlling interest or factor."[66] Thus, boards of directors, committees of the board, and individual directors of bank holding companies registered as Pennsylvania corporations are expressly permitted to consider and adopt policies based on interests beyond those of the shareholders.[67] Therefore, when faced with a takeover attempt, the board of a Pennsylvania bank holding company may take action, even if it has the effect of reducing share value, and justify its decision on the interests of the community.

The Pennsylvania law provides further protection for boards of directors who choose to base decisions on interests other than those of the shareholders.[68] The law creates a presumption that, absent a breach of fiduciary duty, lack or good faith or self-dealing, any action by the board, a committee of the board, or individual director is in the best interest of the corporation.[69] Pennsylvania law provides the directors with an even greater amount of protection from disgruntled shareholders when the board is defending against a hostile takeover attempt.[70] In order to succeed on any claim challenging a decision of the majority of the disinterested directors,[71] which relates to or affects "an acquisition or potential

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of this statute, along with the other portions of Pennsylvania's antitakeover legislation in *Armstrong World Industries, Inc. v. Adams*, 961 F.2d 405 (3d Cir. 1992). The court determined that the claims were not ripe for review. *See id.*

66. Title 15, § 1715(b).

67. *See id.*

68. *See id.* § 1715(d).

69. *See id.*

70. *See id.*

71. "Disinterested director" is defined in section 1715 as

> (1) A director of the corporation other than:
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> (i) A director who has a direct or indirect financial or other interest in the person acquiring or seeking to acquire control of the corporation or who is an affiliate or associate . . ., or was nominated or designated as a director by, a person acquiring or seeking to acquire control of the corporation.
>
> (ii) Depending on the specific facts surrounding the director and the act under consideration, an officer or employee or former officer or employee of the corporation.

Title 15, § 1715(e)(1). A person is not considered to be other than a disinterested director solely by owning shares of the corporation, receiving a distribution made to holders of shares of the corporation, the receipt of consideration or right to retirement compensation for serving as a director, any interests a director may have in retaining their status as director, or any former business or employment relationship with the corporation. *See id.*

or proposed acquisition of control,"[72] an opponent of the board must establish by "clear and convincing evidence"[73] that the directors did not act in good faith.[74]

When presented with an acquisition offer, the board of a bank holding company may choose to reject proposal, citing to the interests and needs of the community as justification for its action.[75] A rejection leaves the would-be acquiror to decide between abandoning the offer or proceeding to mount an assuredly costly hostile takeover attempt. If the would-be acquiror decides to proceed with a hostile takeover attempt, the acquiror must obtain approval from the Board of Governors of the Federal Reserve Board if the acquiror will obtain more than 5% of the voting shares of any bank through acquiring ownership in the bank holding company.[76] The Board of Governors then, in deciding whether to approve the application, must consider consummation of the proposal in light of the needs and convenience of the community.[77]

The board of directors of a target bank holding company, when opposed to any acquisition attempt, may choose to adopt policies to prevent the takeover from succeeding. The board of directors may cite as justification for those actions a factor the Board of Governors must too consider: the interests of the community that would be affected by consummation of the takeover attempt.[78] Thus, in situation involving a hostile takeover attempt of a Pennsylvania bank holding company, both the Board of Governors of the Federal Reserve Board and the board of directors of the target corporation may be basing their decisions, in part, on the needs of the community involved.[79] The legislative scheme allows for the possibility that the Board of Governors and

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§ 1715(d)(2).

72. *Id.* § 1715(d).

73. *Id.*

74. *See id.*; *see also* Michael S. Marshall, Comment, *Beyond the Third Generation: An Analysis of Pennsylvania's Latest Attack on Hostile Takeovers*, 29 DUQ. L. REV. 579, 582 (1991) ("Arguably, the legislature has granted directors a blank check when a takeover attempt looms on the horizon").

75. Mellon's board of directors cited the interests of the community as among factors it considered in deciding to reject The Bank of New York's April 1998 unsolicited bid. *See Bank Scuttles Move for Deal to Buy Mellon*, HARRISBURG PATRIOT, May 21, 1998, at B11.

76. *See* 12 U.S.C. § 1842(a)(3) (1994).

77. *See id.* § 1842(c)(2).

78. *See* 15 PA. CONS. STAT. ANN. § 1715(a)(1) (West 1995).

79. *See* 12 U.S.C. § 1842(c)(2); *see also* title 15, § 1715(a)(1).

the board of directors of a target Pennsylvania bank holding company will disagree as to whether the proposed acquisition is in the best interest of the relevant communities.

Can the Pennsylvania legislature allow boards of directors of holding companies to make decisions based on the needs of the community, even if the Board of Governors disagrees with the directors' determinations concerning the impact a proposed acquisition would have on the relevant community? Or does the Federal Bank Holding Company Act prevent Pennsylvania from allowing boards of directors of corporations registered in the Commonwealth from making such determinations when the corporation is a bank holding company? The next section will explore whether federal law preempts Pennsylvania's fiduciary duty statute as it applies to bank holding companies.

IV. Preemption Analysis

Federal preemptive authority is based on the Supremacy Clause of the United States Constitution.[80] Article VI states that "[T]he Laws of the United States . . . shall be the supreme Law of the Land . . . ."[81] Following the principle first expressed in *McCulloch v. Maryland*,[82] more recent decisions have stated that "it has been settled" that state law that conflicts with federal legislation is "without effect."[83]

Analysis of federal preemption of state action begins with the presumption that state law is not superseded when the state is exercising its traditional powers.[84] The Supreme Court has declared that " '[w]e will interpret a statute to pre-empt the traditional state powers only if that result is 'the clear and manifest purpose of Congress.' "[85]

In the United States, individual states have traditionally had the power to charter corporations,[86] and therefore have possessed the power to define how those corporations are governed.[87]

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80. *See* McCulloch v. Maryland, 17 U.S. (4 Wheat) 316, 405-06 (1819).

81. U.S. CONST. amend. VI, § 2.

82. 17 U.S. (4 Wheat) 316.

83. Cipollone v. Ligget Group, Inc., 505 U.S. 504, 516 (1992) (citing Maryland v. Louisiana, 451 U.S. 725, 746 (1981)).

84. *See* Dept. of Revenue of Oregon v. ACF Industries, Inc., 510 U.S. 332, 345 (1994).

85. *Id.* (quoting Rice v. Santa Fe Elevator Corp., 331 U.S. 218, 230 (1947)).

86. *See* DETLEV F. VAGTS, BASIC CORPORATION LAW 2, (3d ed. 1989); *see also* Chicago Title and Trust Co. v. Forty-Six Wilcox Bldg. Corp., 302 U.S. 120, 124-25 (1937).

87. *See Chicago Title and Trust*, 302 U.S. at 124-25.

According the Supreme Court's decision in *Lewis v. BT Investment Managers*,[88] that the same authority exists where the corporation is a bank holding company, an entity that has received a great deal of attention from Congress. In a decision considering the power of state regulation over bank holding companies in light of the Bank Holding Company Act, the Supreme Court stated that "as a matter of history . . . banking and related financial activities are of profound local concern."[89] Therefore, as is the case with any traditional state power, the preemption analysis begins with the assumption that Pennsylvania has the authority to define the standard by which directors of bank holding companies chartered within the Commonwealth exercise their duties.

The intention of Congress is the "ultimate touchstone" for analyzing the preemptive effect of federal law.[90] Congressional intent may be (1) expressed in the language of the statute, or (2) implicit in the structure and purpose of the legislation.[91] The Bank Holding Company Act contains no provision expressly stating that only the Board of Governors may consider community needs when evaluating the potential effects of a bank holding company acquisition. Thus, if Congress has preempted the states from allowing directors of bank holding companies to consider the same factors the Board of Governors must consider, it must have done so implicitly.

The Supreme Court has applies two tests for determining the existence of implicit preemption.[92] State law is implicitly preempted by federal law if the (1) federal law " 'so thoroughly occupies a legislative field 'as to make reasonable the inference that Congress left no room for states to supplement it' "[93] or (2) state law actually conflicts with federal law.[94] The BHCA itself contemplates certain areas where the states may act in ways that affect bank holding company acquisitions,[95] thus federal law does not so thoroughly occupy the field such that a state may not supplement it with its own legislation. Therefore, in order for implicit preemp-

88. 447 U.S. 27 (1980).

89. *Id.* at 38.

90. Cippollone v. Ligget Group Inc., 505 U.S. 504, 516 (1992).

91. *See id.*

92. *See id.*

93. *Id.* (quoting Fidelity Fed. Sav. & Loan Ass'n v. De la Cuesta, 458 U.S. 141, 153 (1982)).

94. *See id.*

95. *See* 12 U.S.C. § 1842(d)(1)(B) & (D) (1994).

tion to exist, the provisions of Pennsylvania's fiduciary duty statute must actually conflict with the BHCA.

The Supreme Court has stated that an actual conflict between state and federal laws exists when the state law " 'stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.' "[96] The legislative history of the Bank Holding Company Act states that "public welfare requires the enactment of legislation providing Federal regulation of the growth of bank holding companies . . . ."[97] According to the Senate Committee Report, the importance of banking to the national economy required Congress to provide for federal regulation of bank holding companies.[98] In weighing various factors designated by Congress, which include the convenience, needs and welfare of the community, Congress contemplated that Federal Reserve Board regulation would provide that consolidations, mergers, and acquisitions "would be regulated in the public interest."[99] While the BHCA contains nothing expressly addressing the decision-making process of boards of directors of bank holding companies, Congress has, according to the legislative history, given the Federal Reserve Board the responsibility of protecting the public welfare in the field of bank holding company acquisitions.[100]

In addition, in light of the Interstate Branching and Banking Act of 1994, Congress appears to prefer that the states play a minimal role in making policy decisions governing bank holding company acquisitions. The Senate Committee Report on the Interstate Branching and Banking Act of 1994 states that one of the purposes of the amendments to the Bank Holding Company Act made pursuant to the IBBEA is to "eliminate remaining disharmonious local law restrictions on interstate bank holding company acquisitions of banks in different states" in order to

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96. Int'l Paper Co. v. Ouellette, 479 U.S. 481, 491-92 (1987) (quoting Hillsborough County v. Automated Medical Lab., Inc., 471 U.S. 707, 713 (1985)). An actual conflict may also exist where "compliance with both federal and state regulations is a physical impossibility . . . ." Florida Lime & Avocado Growers, Inc. v. Paul, 373 U.S. 132, 142-43 (1963). No such conflict exists between the BCHA and the Pennsylvania fiduciary duty law because both the Board of Governors and the boards of directors could agree. There is "no inevitable collision" between the federal and Pennsylvania laws. *See id.* at 143.

97. S. REP. NO. 1095, at 1 (1955), *reprinted in* 1956 U.S.C.C.A.N. 2482, 2482.

98. *See id.*

99. *Id.* at 10.

100. *See id.*

reduce the barriers to interstate banking.[101] The legislative history indicates that in passing the IBBEA, Congress contemplated restricting state control over interstate bank acquisitions.[102]

By giving the power to make decisions for the community to boards of directors of corporations, the Pennsylvania law has the potential to create a barrier to the purpose of Congress to eliminate the "disharmonious local law restrictions on interstate bank holding company acquisitions . . . ."[103] Furthermore, Pennsylvania allows boards of directors to adopt policies and make determinations for the community, a practice that, if done by a state body concerning a bank holding company acquisition, would be disregarded by the Federal Reserve Board.[104]

When Congress enacted the IBBEA in 1994, Pennsylvania's current fiduciary duty statute was in effect.[105] There is no mention of state corporation laws or their impact on potential bank holding company acquisitions in the history of the IBBEA. Thus, it appears that by passing the IBBEA, Congress was not concerned with varying state corporation laws and the nonuniform impact they may have on bank holding company acquisition attempts. Congress' concern may have been only with ending direct state legislation that restrained interstate bank acquisitions, such as the regional and reciprocity laws.[106]

There is no evidence however, that Congress was aware of Pennsylvania's fiduciary duty statute. Moreover, when considering the preemptive effect of federal law, the Supreme Court is "reluctant to draw inferences from Congress's failure to act."[107] Therefore, Congress' failure to address an issue is not determinative of its intent.[108]

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101. S. REP. NO. 103-240, at 10 (1994).

102. *See id.*

103. *Id.* Unlike those of most States, Pennsylvania's fiduciary duty law contains no provision requiring boards of directors to consider shareholder interests the primary concern upon an exercise of their duties. *See* Meyerson & Alpuche, *supra* note 4, at 117. Only Indiana has enacted a similar law. *See id.*; *see also* IND. CODE ANN. § 23-1-351(d) & (f) (Michie 1995).

104. *See* 12 U.S.C. § 1842 (d)(1)(A) (1994).

105. The current statute was enacted on December 19, 1990. *See* notes to 15 PA. CONS. STAT. ANN. § 1715 (West 1995).

106. *See* 12 U.S.C. § 1842(d)(1)(A); *see also* S. REP. NO. 103-240, at 10 (1994).

107. Schneidewind v. ANR Pipeline Co., 485 U.S. 293, 306 (1988).

108. *See id.*

Nonetheless, an expression by Congress addressing preemption, stated in the language of the statute, governs the statute's preemptive scope.[109] The Supreme Court has stated that "[w]hen Congress has considered the issue of preemption and has included in the enacted legislation a provision explicitly addressing that issue, and when that provision provides a 'reliable indicium of congressional intent with respect to state authority . . .' there is no need to infer congressional intent to pre-empt state laws from the substantive provisions."[110] While the inclusion of an express clause defining the preemptive reach of a federal statute does not determine that implied preemption cannot exist,[111] it may support an inference that an express clause forecloses preemption.[112]

Upon passage of the Bank Holding Company Act in 1956, Congress included a section reserving the rights of states to govern bank holding companies.[113] Despite the change in emphasis away from state regulation in the IBBEA, Congress has left this provision largely unchanged.[114] Section 1846 of the BHCA states that "No provision of this chapter shall be construed as preventing any State from exercising such powers and jurisdiction which it now has or may hereafter have with respect to companies, banks, bank holding companies, and subsidiaries thereof."[115] With the inclusion of this section, the Supreme Court has determined that "Congress' concern was to define the extent of the federal legislation's pre-emptive effect on state law."[116] The Supreme Court found that section 1846 preserves existing State powers.[117] Therefore, because states have traditionally possessed the power to

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109. *See* Cippollone v. Ligget Group, Inc., 505 U.S. 504, 517.

110. *Id.* at 517 (quoting Malone v. White Motor Corp., 435 U.S. 497 (1978)).

111. *See* Freightliner Corp. v. Myrick, 514 U.S. 280, 287-88 (1995).

112. *See id.* at 288.

113. *See* 12 U.S.C. § 1846 (1994); *see also* S. REP. NO. 1095, at 22 (1955), *reprinted in* 1956 U.S.C.C.A.N. 2482, 2504.

114. *See* 12 U.S.C. § 1846(b). The only substantial change was the addition of part b, which provides that state taxation authority is not to be affected by the Bank Holding Company Act. *See id.*

115. *Id.* § 1846(a).

116. Lewis v. BT Inv. Managers, Inc., 447 U.S. 27, 49 (1980).

117. *See id.* State and federal courts have found that section 1846 ensured state power to prohibit bank holding companies within their respective jurisdictions. *See, e.g.,* Commercial Nat'l Bank of Little Rock v. Board of Governors of Fed. Reserve Sys., 451 F.2d 86 (8th Cir. 1971); *see also* Security Nat'l Bank & Trust Co. v. First West Virginia Bancorp, Inc., 277 S.E.2d 613, 615 (W. Va. 1981).

charter corporations,[118] and thus define how directors may exercise their fiduciary duty,[119] section 1846 appears to ensure that the states maintain their authority over corporations, even if the corporation is a bank holding company. While the Board of Governors is given the responsibility to decide which acquisitions will produce outcomes in accord with the needs and convenience of the community,[120] and Congress has recently enacted legislation that indicates an intention to severely limit state laws preventing interstate bank acquisitions,[121] Congress has not indicated a "clear and manifest" purpose to prevent States from allowing boards of directors to consider the interests of the community in the exercise of their duties.

Despite the apparent conflict that remains if Congress has not preempted the Pennsylvania law, the two laws can be reconciled. In the past, the Board of Governors has adopted a policy of neutrality toward an acquisition planned to occur through hostile means.[122] The Board has stated that under the Bank Holding Company Act it must apply "the statutory criteria equally in the case of applications supported by the management of the acquired company as well as in those that are opposed by management."[123] Thus, the Board of Governors may grant approval for a hostile acquisition to occur, whether or not the hostile attempt is ultimately successful.[124] While the Board of Governors adopted its policy of neutrality prior to the passage of the Interstate Branching and Banking Act,[125] the Board's approach is still consistent with the IBBEA. An amendment to the Bank Holding Company Act replacing the Douglass Amendment, enacted as part of the IBBEA states that "[t]he Board may approve an application . . . without regard to whether such transaction is prohibited under the law of

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118. *See* VAGTS *supra* note 86; *see also* Chicago Title and Trust Co. v. Forty-Six Wilcox Bldg. Corp. 302 U.S. 120, 124-52 (1937).

119. *See Chicago Title and Trust*, 302 U.S. at 124-25.

120. *See* 12 U.S.C. § 1842(c)(2).

121. *See* S. REP. NO. 103-240, at 10 (1994) (stating that one of the purposes of the IBBEA is to eliminate local law restrictions on interstate bank holding company acquisitions).

122. *See* Meyerson & Alpuche, *supra* note 4, at 81; *see also* The Bank of New York Co., Inc., 74 Fed. Res. Bull. 257, 259 (1988).

123. The Bank of New York Co., Inc., 74 Fed. Res. Bull. at 259. The Board employs a higher degree of scrutiny when considering an application in which the management of the organization to be acquired opposes the application. *See id.*

124. *See id.*

125. *See id.* at 257 (decision of the Board issued in 1988).

any State."[126] Thus, the Board may perform its responsibilities and fulfill its obligations while ignoring the Pennsylvania law and the decisions made by the directors of the target bank holding company.

The case remains that directors of Pennsylvania bank holding companies may have the ability to second guess the decision of the Board of Governors. The Board of Governors could approve an application for an acquisition of a Pennsylvania bank holding company only to have the management of the target bank holding company succeed in avoiding the hostile attempt, and cite as justification for their actions, at least in part, the needs of the community, a factor the Board must have already considered. Regardless of the possibility of this scenario, the Board of Governors maintains the ability to make the ultimate decision over whether a bank holding company acquisition will occur. While the directors of a target Pennsylvania bank holding company may prevent consummation of an acquisition approved by the Board of Governors, an acquisition, even if supported by the management, cannot occur without the approval of the Board. Thus, the Congressional policy favoring Federal Reserve Board regulation over the expansion of bank holding companies remains fulfilled.

V. Conclusion

The long list of factors that boards of directors are expressly permitted to consider under Pennsylvania's fiduciary duty statute may make the question of preemption largely academic. In addition to permitting consideration of the interest of the community, Pennsylvania's fiduciary duty law allows directors, committees of directors, and boards of directors to consider also the interests of employees, suppliers, customers, creditors and "[a]ll other pertinent factors" in the exercise of their duties.[127] Thus, even if directors of Pennsylvania bank holding companies could not take action based on the interests of the community, they would have a seemingly endless variety of topics to choose from upon which they may justify their decisions.

The fiduciary duty statute, unlike the legislation introduced in the Assembly during the 182nd Session in 1998, does not ensure that a Pennsylvania entity, whether public or private, will consider

126. 12 U.S.C. § 1842(d)(1)(A) (1994).
127. *See* 15 PA. CONS. STAT. ANN. § 1715(a) (West 1995).

the needs of the Commonwealth's communities when considering a takeover bid. However, even if the Pennsylvania legislature had been successful in granting the State Banking Department the authority to measure a proposed acquisition's impact on the community and either prevent or allow consummation of the proposal based on its determination, the bill would be of questionable validity at best in light of the IBBEA.[128] Nonetheless, the proponents of the bill may find some consolation in the fact that they may have escaped federal preemption by delegating the power to make decisions for the future of the Commonwealth's communities to the boards of directors of the bank holding companies chartered in the Commonwealth. Perhaps the legislature will remain satisfied with trusting the boards of directors to protect and promote community interests.

Despite statements from both Congress and the Pennsylvania legislature regarding the special importance of banking in daily life,[129] both governments allow the public at large to exercise very minimal, if any, direct or indirect control over policy governing bank holding company acquisitions and in determining which proposals will further the interests of the community involved.[130] One vote the community does maintain though, comes not from the ballot box, but from the checkbook, the wallet, and the savings portfolio, and in making the ultimate determination as to which banks serve the community best perhaps that is the vote that matters most.

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128. *See* 12 U.S.C. § 1842(d)(1)(A) (stating that the Board of Governors may approve an application for an acquisition of an adequately capitalized and managed bank holding company "without regard to whether such transaction is prohibited under the law of any State").

129. *See* S. REP. NO. 1095, at 1, 2 (1955), *reprinted in* 1956 U.S.C.C.A.N. 2482, 2482, 2483; *see also* 36 PA. LEGIS. J.-S. 2050, 2052, 182nd Legis. Sess. (June 8, 1998).

130. The Board of Governors of the Federal Reserve Board is composed of seven members appointed by the President with the advice and consent of the he Senate. *See* 12 U.S.C. § 241 (1994).